

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the Dr Beyers Naude Local Municipality

Report on the audit of the financial statements

Disclaimer of opinion

1. I was engaged to audit the financial statements of the Dr Beyers Naude Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2018, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. I do not express an opinion on the financial statements of the municipality. Due to the significance of the matter described in the basis for disclaimer of opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for disclaimer of opinion

Limitations on the financial statements

3. I was unable to obtain sufficient appropriate audit evidence regarding the financial statements as a whole, as the financial statements were presented for audit purposes without accurate and complete underlying accounting records. I was unable to audit the financial statements by alternative means. Consequently, I was unable to determine whether any adjustments relating to the financial statements as a whole were necessary.

Other matters

4. I draw attention to the matters below:

Withdrawal from the audit engagement

5. Due to the limitation imposed on the scope of the audit by management, I have disclaimed my opinion on the financial statements. Were it not for the legislated requirement to perform the audit of the municipality, I would have withdrawn from the engagement in terms of the International Standards on Auditing (ISAs).

Unaudited disclosure notes

6. In terms of section 125(2)(e) of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), the municipality is required to disclose particulars of non-compliance with this legislation. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

Unaudited supplementary information

7. The supplementary information set out on pages x to x does not form part of the annual financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not report thereon.

Responsibilities of the accounting officer for the financial statements

8. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the MFMA and the Division of Revenue Act of South Africa, 2017 (Act No. 3 of 2017) (Dora), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
9. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

10. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
11. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

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| Report on the audit of the annual performance report |
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Introduction and scope

12. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report. I performed procedures to raise findings but not to gather evidence to express assurance.

13. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
14. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected objectives presented in the annual performance report of the municipality for the year ended 30 June 2018:

| Objectives | Pages in the annual performance report |
|---|--|
| KPA 2 – basic service delivery and infrastructure development | x – x |
| KPA 3 – local economic development | x – x |

15. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
16. I did not raise material findings on the usefulness and reliability of KPA 2 – basic service delivery and infrastructure development, and KPA 3 – local economic development.

Other matters

17. I draw attention to the matters below.

Achievement of planned targets

18. Refer to the annual performance report on pages x to x and x to x for information on the achievement of planned targets for the year and explanations provided for the underachievement of a number of targets.

Adjustment of material misstatements

19. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of KPA 2 – basic service delivery and infrastructure development. As management subsequently corrected the misstatements, I did not raise any material findings on the usefulness and reliability of the reported performance information.

Introduction and scope

20. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to raise findings but not to gather evidence to express assurance.
21. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements and annual report

22. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Supporting records that could not be provided resulted in the financial statements receiving a disclaimer of audit opinion.

Strategic planning and performance management

23. The integrated development plan did not reflect financial plans, as required by section 26(h) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) and municipal planning and performance management regulation 2(3)(a).
24. The service delivery and budget implementation plan for the year did not include the monthly operational and capital expenditure by vote, as required by section 1 of the MFMA.

Expenditure management

25. I was unable to obtain sufficient appropriate audit evidence that money owed by the municipality had always been paid within 30 days, as required by section 65(2)(e) of the MFMA.
26. I was unable to obtain sufficient appropriate audit evidence that payments from the municipality's bank account were approved by the accounting officer, as required by section 11(1) of the MFMA.
27. Reasonable steps were not taken to ensure that the municipality implemented and maintained an effective system of expenditure control, including procedures for the approval of funds, as required by section 65(2)(a) of the MFMA. An adequate management accounting and information system was not in place, which recognised expenditure when it was incurred as well as creditors, as required by section 65(2)(b) of the MFMA.
28. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified, as indicated in the basis for disclaimer paragraph.
29. Reasonable steps were not taken to prevent fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the fruitless and wasteful expenditure could not be quantified, as indicated in the basis for disclaimer paragraph.
30. Reasonable steps were not taken to prevent unauthorised expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the unauthorised expenditure could not be quantified, as indicated in the basis for disclaimer paragraph.

Revenue management

31. A tariff policy was not adopted for the levying of fees for the provision of municipal services, as required by section 74(1) of the MSA and section 62(1)(f)(i) of the MFMA.
32. A credit-control and debt-collection policy was not adopted, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of the MFMA.
33. A policy on the levying of rates on rateable property within the municipality was not adopted, as required by section 3(1) of the Municipal Property Rates Act of South Africa, 2004 (Act No. 6 of 2004) and section 62(1)(f)(ii) of the MFMA.
34. An adequate management, accounting and information system was not in place to account for revenue, debtors and receipts of revenue, as required by section 64(2)(e) of the MFMA.
35. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
36. I was unable to obtain sufficient appropriate audit evidence that revenue due to the municipality was calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.
37. I was unable to obtain sufficient appropriate audit evidence that accounts for municipal tax and charges for municipal services or service charges were prepared on a monthly basis, as required by section 64(2)(c) of the MFMA.
38. I was unable to obtain sufficient appropriate audit evidence that interest had been charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

Conditional grants

39. Performance in respect of programmes funded by the municipal infrastructure grant was not evaluated, as required by section 12(5) of Dora.
40. I was unable to obtain sufficient appropriate audit evidence that the Municipal Infrastructure Grant was spent for its intended purposes in accordance with the applicable grant framework, as required by section 17(1) of the Division of Revenue Act (Act 3 of 2017).

Asset management

41. The municipality did not establish an investment policy that was adopted by the council, as required by section 13(2) of the MFMA.
42. I was unable to obtain sufficient appropriate audit evidence that all investments were made in accordance with the requirements of the investment policy, as there was no specific investment policy in place and the one policy that included a section about investments had not been approved by the council, as required by municipal investment regulation 3(3).

Liability management

43. An adequate management, accounting and information system was not in place to account for liabilities, as required by section 63(2)(a) of the MFMA.
44. An effective system of internal control for liabilities (including a liability register) was not in place, as required by section 63(2)(c) of the MFMA.
45. Short-term debt relating to the bank overdraft was incurred for reasons other than those allowed as per section 45(1) of the MFMA.

46. Short-term debt relating to the bank overdraft was incurred without a resolution of the municipal council approving the debt agreement, in contravention of section 45(2)(a) of the MFMA.
47. Short-term debt relating to the bank overdraft was not repaid within the financial year, as required by section 45(4) of the MFMA.

Consequence management

48. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
49. Losses resulting from unauthorised expenditure were not recovered from the liable person, as required by section 32(2)(a) of the MFMA.
50. The authorisation of unauthorised expenditure amounting to R17,1 million was not done through an adjustment budget, as required by section 32(2)(a)(i) of the MFMA.
51. Irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
52. Losses resulting from irregular expenditure were not recovered from the liable person, as required by section 32(2) of the MFMA.
53. Cases of irregular expenditure that constituted a criminal offence were not reported to the South African Police Service, as required by section 32(6).
54. Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
55. Losses resulting from fruitless and wasteful expenditure were not recovered from the liable person, as required by section 32(2)(b) of the MFMA.

Human resource management

56. I was unable to obtain sufficient appropriate audit evidence that the municipal manager disclosed financial interests within 60 days from the date of appointment, as required by regulation 36(1)(a) on the appointment and conditions of employment of senior managers.
57. I was unable to obtain sufficient appropriate audit evidence that senior managers disclosed financial interests within 60 days from the date of appointment, as required by regulation 36(1)(a) on the appointment and conditions of employment of senior managers.
58. I was unable to obtain sufficient appropriate audit evidence that senior managers previously dismissed for financial misconduct were only re-appointed after the expiry of a 10-year term, as required by section 57A(1) of the MSA.
59. An approved staff establishment was not in place, as required by section 66(1)(a) of the MSA.
60. I was unable to obtain sufficient appropriate audit evidence that appropriate systems and procedures to monitor, measure and evaluate the performance of staff were developed and adopted, as required by section 67(1)(d) of the MSA.

Procurement and contract management

61. Some goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations, in contravention of supply chain management (SCM) regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.

62. Some quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
63. Some goods and services with a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
64. Competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2). Similar non-compliance was also reported in the prior year. This non-compliance was identified in the procurement processes for the key project – 86/2017: the construction and refurbishment of stormwater infrastructure in Umasizakhe and Kroonvale residential areas.
65. Some contracts were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
66. Some contracts were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of SCM regulation 43.
67. Bid documentation for the procurement of commodities designated for local content and production did not stipulate the minimum threshold for local production and content, as required by preferential procurement regulation 8(2) of 2017.
68. Some commodities designated for local content and production were procured from suppliers who did not submit a declaration on local production and content, as required by the Preferential Procurement Regulations 8(5) of 2017.
69. Some commodities designated for local content and production were procured from suppliers who did not meet the prescribed minimum threshold for local production and content, as required by preferential procurement regulation 8(5) of 2017.
70. Awards were made to providers who were in the service of the municipality or whose directors were in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM regulation 44. Furthermore, providers failed to declare that they were in the service of the municipality, as required by SCM regulation 13(c).
71. Sufficient information was not provided to confirm that awards were made to providers who were in the service of other state institutions or whose directors were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44.
72. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e), the code of conduct for councillors issued in terms of the MSA, or the code of conduct for staff members issued in terms of the MSA.
73. Persons in the service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e), the code of conduct for councillors issued in terms of the MSA, or the code of conduct for staff members issued in terms of the MSA.
74. SCM officials who, or other SCM role players whose close family members, partners or associates, had a private or business interest in contracts awarded by the municipality participated in the process relating to that contract, in contravention of SCM regulation 46(2)(f).

Other information

75. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the audit committee's report, mayor's foreword and executive summary, municipal manager overview. The other information does not include the financial statements, the auditor's report thereon and those selected programmes presented in the annual performance report that have been specifically reported on in the auditor's report.
76. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
77. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected objectives presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
78. There were no material inconsistencies identified.

Internal control deficiencies

79. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the disclaimer of opinion, the findings on the performance report and the findings on compliance with legislation included in this report.
- Leadership did not exercise oversight over financial, performance and compliance reporting, as the annual financial statements, annual report and compliance reporting were not adequately reviewed, which contributed to the material findings reported.

The municipality did not maintain a proper record management system for electronic records, or for the timely retrieval thereof, as evidenced by the fact that the annual financial statements were not supported by relevant schedules and supporting documentation. Furthermore, the general ledger and trial balance did not agree to the annual financial statements, and numerous instances of material non-compliance with legislation were identified.

- The audit committee did not review the annual financial statements and annual performance report in the current year, as it was submitted late for their review.
- The internal audit unit lacked the capacity required to effectively perform their duties, as they had limited time to review the annual financial statements.

Auditor-General

East London

7 December 2018



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence